APPENDIX A

Opinion of the Court of Appeals

July 18, 1967

Before SCHNACKENBERG, CASTLE and FAIRCHILD, *Circuit Judges.*

CASTLE, *Circuit Judge.* The plaintiff-appellant, Young-Peterson Construction, Inc., brought this diversity action in the District Court against The Potomac Insurance Company of the District of Columbia, defendant-appellee, seeking to recover the value of four truck tractors and dump-type trailers under the "theft" clause of an insurance policy deefndant issued to the plaintiff. The cause was tried to a jury which returned a verdict for the defendant upon which the court entered judgment. The plaintiff appealed and contends the court committed reversible error in its denial of plaintiff's motion for a directed verdict and its motion for judgment notwithstanding the verdict or, in the alternative, for a new trial.

The main contested issue precipitated by plaintiff's appeal, and about which its principal contention centers, is whether there is any evidence to support a conclusion by the jury that the taking involved was in the exercise of a good faith claim of right.

The insurance policy issued by the defendant listed the motor vehicle equipment here involved and contained a clause insuring against loss or damage "caused by theft, larceny, robbery or pilferage". Plaintiff contends that the four truck tractors and trailers in question were taken by Robert Holtman on or about April 24, 1959, from a service-station storage yard at Homewood, Illinois, transported to Phoenix, Arizona, and there sold by Holtman, under circumstances constituting a theft rather than a taking in a good faith exercise of a claim of right.

Plaintiff, an Illinois corporation, was organized by J. Bernard Mullen, Jr. and Mark Willing, Jr. in March of 1958 to perform a highway construction sub-contract. Allen Young was employed as the president of the corporation. He was not, however, a stockholder, nor did he ever make any capital contribution to the corporation. The sub-contract was completed in October, 1958, and although by its terms Young's written employment contract as president and general manager of the plaintiff corporation then expired, he continued to assist in its activities in connection with finishing two related hauling jobs the corporation performed and thereafter went to Arizona in an effort to locate work on which the plaintiff's equipment could be utilized. The plaintiff had no active vice-president, and a president to succeed Young was not named until after the events which are here pertinent.

The five truck tractors and trailers which the plaintiff had purchased to perform the highway construction sub-contract were stored in December 1958 on a farm at McHenry, Illinois. In April 1959 they were moved to the service-station lot at Homewood.

The testimony relevant to the circumstances leading to and surrounding Holtman's removal of four of the truck tractors and their trailers from the Homewood premises presents conflicts. But the resolution of these conflicts and the credibility questions incident thereto was peculiarly within the province of the jury. The scope of our review, insofar as the sufficiency of the evidence is concerned, is here limited to a determination of whether the evidence, and all reasonable inferences that may be drawn therefrom, considered in the light most favorable to the defendant, supports the verdict of the jury.

The plaintiff contends that the defendant's defense that Holtman's taking of the motor vehicle equipment was in the exercise of a good faith claim of right, and therefore not within the scope of the coverage afforded by the policy, is defective in two respects. First, that the claim of right defense is available only where the taker is a person having a pre-existing close relationship

of use and ownership to the property taken which precedes that of the person from whom the property was taken. And, second, that in the instant case the essential element that the taker be in the exercise of good faith in his claim of right is lacking—that the record negates good faith on the part of Holtman.

It is conceded that Holtman never had any relationship of use or ownership of any of the vehicles, or interest therein, which preceded that of the plaintiff. It is on the basis of the absence of any such factor that plaintiff makes its first contention that the claim of right defense is unavailable to the defendant. Plaintiff cites nine cases[1] which have been concerned with the development and application of the claim of right doctrine as a defense to the liability of an insurer under the "loss by theft" coverage of its policy. Plaintiff contends that these cases authorize the claim of right defense only where the taker, in addition to being in good faith, was taking a vehicle as to which he had a prior close relationship of use and ownership. While these cases are illustrative of factual situations where such a factor was present, we perceive nothing in the rationale upon which these decisions are based which makes the element of such a prior relationship to or ownership of the property taken a *sine qua non* to the availability of the claim of right defense to the insurer of the property. In our opinion the defense is available where the taking is by any person acting under an honest belief that he is entitled to possession of the property. Insurance Law and Practice, Appleman, §3211, p. 356.

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[1] *Laporte Motor Company* v. *Firemen's Ins. Co., of Newark, N.J.*, 209 Wisc. 397, 245 N.W. 105; *Durback* v. *Fidelity and Guarantee Co.*, 85 Atl. 2d 315, 17 N.J. Sup. 160; *Bowling* v. *Hamblen County Motor Co.*, 16 Tenn. App. 52, 66 S.W. 2d 229; *Bigus* v. *Pacific Coast Casualty Co.*, 129 S.W. 982, 145 Mo. App. 170; *Rush* v. *Boston Insurance Co.*, 150 N.Y. 457, 88 Misc. 48; *State Assurance Underwriters of Providence Fire Ins. Co.* v. *Miller*, 58 So. 2d 532; *South Carolina Ins. Co.* v. *Jackson*, 117 S.E. 2d 878; *Talasek* v. *Travelers Fire Ins. Co.*, 242 F. 2d 748; *Reece* v. *Motors Ins. Corp.*, 116 F. Supp. 394.

We turn to consideration of whether, viewing the record most favorably to the defendant, there is any evidence which would warrant a conclusion by the jury that Holtman acted in good faith and under color of right in his taking of the four truck tractors and their trailers. In this connection there is evidence that before Holtman removed the vehicles from the Homewood service-station lot, Young, who had possession of the title documents to the vehicles, had, over his signature as president of the corporation, executed assignments of the titles from plaintiff to Holtman as security for loans and advances made by Holtman, and had delivered the title certificates and the keys to the vehicles to Holtman. Prior to removing the vehicles, Holtman had conversations with Mullen, and with an attorney for the plaintiff, in which he informed them he had title to the vehicles and had come to get them. Neither questioned the authority of Young to act for the plaintiff but advised Holtman that Young couldn't have given him title to the vehicles because they belonged to a bank which had liens on them. The title papers disclosed no liens and Holtman proceeded to remove the vehicles after first soliciting and obtaining the presence of a local police officer to stand by in event of any trouble. The vehicles were openly transported in caravan to Arizona where Holtman resided.

The record discloses that Young, while attempting to secure construction work in Arizona on which the plaintiff's motorized equipment could be put to use, contacted Holtman at the latter's residence in Phoenix. Young had been told that Holtman also had been a sub-contractor on the Illinois project. Young subsequently made representations to Holtman to the effect that the plaintiff was about to become the prime contractor in connection with a project for the construction of housing for the elderly at Phoenix; that plaintiff would do the site-leveling, dirt moving, sewer and road work itself, but would sub-let the balance of the work. There is testimony that the loans and other advances made by Holtman at Young's request, and for which the assignments of title

to the truck tractors and trailers were given as security, approximated $40,000.00. A substantial portion of the money advanced by Holtman was, according to his understanding of Young's representations, a loan to plaintiff to be used for a payment in connection with the housing development project on which plaintiff was to be the prime contractor, in return for which loan Holtman was to receive a 25% interest in the plaintiff and in addition was to be a sub-contractor on the dirt moving involved.

It is not necessary to an application of the claim of right defense that the evidence establish that the taker had a valid right to take the property. Consequently, we are not here concerned with what actual and ultimate legal rights or obligations were created between plaintiff and Holtman by the transactions involved. Nor need we consider and determine the question of Young's actual authority to bind the plaintiff corporation or whether all of the advances made by Holtman may have resulted in the creation of obligations within the scope of that authority.

We are, however, of the opinion that there is evidence from which the jury could have reasonably concluded that Holtman's taking of the truck tractors and trailers was in a good faith exercise of a claim of right based on the assignments of title which had been given to him. The taking was therefore not within the "loss by theft" coverage afforded by the policy issued by the defendant.

In connection with the denial of its motion for a new trial the plaintiff makes certain additional contentions asserting error in the giving of an instruction to which it objected, error arising from comment made by the trial judge in the course of the trial, and error in the court's permitting an amendment to defendant's answer on the first day of trial setting forth additional affirmative defenses. Plaintiff also complains of the conduct of the defendant in interviewing plaintiff's handwriting expert in the absence of plaintiff's counsel after a previously scheduled discovery deposition of the witness had been

continued. The taking of the deposition was subsequently abandoned. We have considered all of these contentions and find them lacking in merit in that none of the matters complained of reveal any error, on the record here involved, which would require reversal. No useful purpose would be served by extending this opinion to discuss them. Suffice it to observe that the trial court's refusal to grant a new trial was not an abuse of discretion. *Hardware Mutual Casualty Company* v. *Chapman*, 7 Cir., 272 F. 2d 614, 617.

The judgment order appealed from is affirmed.

AFFIRMED.

APPENDIX B

Judgment Order of the Court of Appeals Entered July 18, 1967

This cause came on to be heard on the transcript of the record from the United States District Court for the Northern District of Illinois, Eastern Division, and was argued by counsel.

On consideration whereof, it is ordered and adjudged by this court that the judgment order of the said District Court in this cause appealed from be, and the same is hereby, AFFIRMED, with costs, in accordance with the opinion of this Court filed this day.

Order of the Court of Appeals on Petition for Rehearing Entered August 28, 1967

It Is Ordered by the Court that the petition for a rehearing of this cause filed by the plaintiff-appellant herein be, and the same is hereby DENIED.

APPENDIX C

Testimony of David Peck

[By Mr. Williams, attorney for Potomac Insurance Co.]

"Q. Had you known from any source whatsoever, Mr. Mullen or otherwise, on April 19, 1959 that the titles to these four trucks were in the possession of a third person not an employee, not an officer in the company, along with the keys back of these titles the, what appeared at least to be, the signature of the President of the company endorsing them over to someone else existed and that the titles indicated no liens on the face of the titles, would you have issued this insurance?" (App. 174-5).

After objection and ruling by the court, the court restated the question as follows:

"The Court: Do you understand the question? The question is, suppose Mr. Mullen himself had told you that these trucks which you had insured which belonged to the corporation, are trucks, the keys of which have been given over by the President to a third party and the titles of which have been forged or misrepresentations have been based on them, 'but still I want you to put insurance on them', would you have put insurance on them?"

The Witness: If he—

The Court: If he had told you that.

The Witness: That the titles are forged?

The Court: Yes.

The Witness: No, I don't think I would have.

The Court: Of course you wouldn't.

The Witness: I didn't quite get—

The Court: Even for Mr. Mullen?

The Witness: No. I didn't get the forgery aspect. That is what I was wondering about.

By Mr. Williams:

Q. Well regardless of whether you knew they were forged or not, as long as you knew that they were in dispute—

Mr. Cook: I again object. This is all argument.

Mr. Williams: All right.

Mr. Cook: This witness—

"The Court: He may ask the question: 'Even if Mr. Mullen said not that they were forged but that the titles were in dispute, would you have placed insurance on them for him, if he told you—'

The Witness: I would have had to discuss this, I think, with the insurance company or with other parties.

The Court: You wouldn't have bound the company without first discussing it with the company, isn't that correct?

The Witness: I don't think so, no.

The Court: This is the point which he seeks to make. It is hypothetical. He has a right—

The Witness: No, I think I would have to go along—if I knew that this was an illegal procedure, I don't think in fairness to the insurance company—I would have to discuss it further.

[By Mr. Williams]:

Q. All right. One more question.

You have been a long time friend of Mr. Mullen, have you not, socially and otherwise, for twenty years?

A. Correct.

Mr. Williams: That is all." (App. 176-177)

APPENDIX D

Objection to Instruction on Third Affirmative Defense Based on Section 766 of the Insurance Code

Mr. Cook: That is correct. We understand that. We also understand that the statutory law, which has now been given to us, says that for the insurance company to stand on that proposition, then it must assert that it has a declaration of that condition.

There is no such declaration in this case. It has not been proved from the witness stand. There is no documentation on it. It is not in the original policy. There is nothing that could be said to bring it within this cloudy framework that they have been arguing during the course of this trial that somehow Mr. Mullen should have advised the company that at the time he called Dave Peck the insurance title supposedly had been assigned by Young and supposedly the keys had been delivered to Holtman.

That can only be an effective and affirmative and positive defense on one condition, that that condition of Section 766 be applied.

Now, I would like to read, if I may—now, this is the insurance code. I would like to hand it up to the Court, if the Court please—

The Court: No, I would rather not see it because I have said again and again the laws of Illinois are not to be brought in to aid either side in this.

Mr. Cook: This eliminates the third affirmative defense.

The Court: This defense No. 3 I drafted was totally without concern for the insurance law of Illinois.

Mr. Cook: But it has to be related to their affirmative defense.

The Court: It is simply an old equitable defense that grows out of the law of contracts, fraud in the inception. It will void any contract. Any law of Illinois notwithstanding, it will always void a contract. If there was, I don't see where there is too much room for them to argue it, that there was.

Mr. Cook: I think it is grossly unfair to this plaintiff—

The Court: But there has been some evidence of fraud. There is some testimony from a witness whom you produced to the effect that had he known certain things, if they could have been known by the insurer and transmitted to him, he wouldn't have written the binder.

The Court: Now, the job for you gentlemen to do is to argue the facts.

Mr. Cook: But the facts within the law, if the Court please—

The Court: Tell the jury that the plaintiff didn't know these things, that these things weren't true anyway, that the plaintiff didn't know them and, therefore, there was no fraud in the inception. He will be yelling that there will be fraud. This is the way to do it.

Mr. Cook: Section 766 is applicable to insurance contracts. They are governed by statute. There are two volumes of the Illinois Code which relate to them.

We understand what the rules are in relation to fraud, but I think counsel indicated in his statement in which he described this section that he was relying on that it had come in because of the abuse of this defense, which the Court is now permitting to go to the jury, in other

words, a nebulous cloud that somehow the insured is involved in.

It says that these insurance companies when they are writing insurance, if they choose to be protected by a fraud in the declaration, then they shall state that in the declaration. That is the purpose of this statute. It overrides the common law in this kind of a special contract which is fully and completely regulated by our statutes.

I think that to permit that to go to the jury in this case would be an erroneous application of a general doctrine of contract law, which has now been overridden by statute as it relates to the specific type of contract we are dealing with. I can also cite Fletcher Corporations, which deals with the question of the fraudulent president, if this was the case, in which it says again this does not bind the corporation, this knowledge is not imputed to the corporation. There should be an instruction on that. I refer the Court, if I may, to Section 818, Section 819 and Section 820 of Fletcher in which there is a host of cases dealing with this question.

Basically and fully, our proposition, our case, on question of the fraud in the declarations, if there was such, and in this argument, must be controlled by this statutory scheme. We have no right to go beyond it. We are bound by the law in this courtroom.

The Court: Counsel has made his position excellently well understood.

Mr. Cook: Forgive me for making it vehemently, if the Court please, but I think it is an area in which damage will be done to the plaintiff in this case and it is an area which—

The Court: I differ with counsel. This is an area in which counsel can gain great strength on his case by the way he handles his argument. I assure counsel for both sides, even though I limit the arguments in time, that I shall consider the loser the one who fails to utilize the genius of arguing of his case to the jury and not the one who thinks that he has not gotten the instructions slanted his way. I am going to go right down the middle on these instructions and the fewer I give the better.

Let's make it a simple law case. You know, this is the kind of a case which should never be tried with a jury anyway. You should have tried it before me. However, you have it before a jury and I am not going to give them a whole lot of it—I am not going to send them through a four-year course in law or a three-year course in law in 20 minutes. It can't be done. Their instructions are just going to have to be the barest, simplest instructions and you will have to take it from there. This is the tragedy of the use of the system of instructing a jury as to the law in a case that should be before chancery and would have been except for our constitutional provision which makes it triable before a jury.

I feel sorry for the jury if I have to give them all of these instructions that have been proposed. I would do no more than confuse them and place both parties at the jeopardy of a confused jury. This jury has a basic understanding of simple principles about law and there is no reason why those simple principles, with the splendid oratory of counsel for both sides, can't be so clearly brought out in the minds of the jury that they will be able to come down with what is in fact the fair and honest and best decision in the case. When I began looking at those last night and studying them again and again going

over them, I recognized that, in the first place, that more in any recent case that there had been a seeking of importuning by both sides to get the instructions quite slanted in either directions, primarily because the theories of the case were somewhat difficult to grasp from the very outset and it began to develop, crystallize to the point where they were understood by counsel and the Court as the case progressed; but I can't help you with these instructions, I have to leave you out here, both sides out here, on these little limbs yourselves.

I am going to give simple instructions to the jury, basic, simple instructions, and allow you to carry on. The rest of it can be in the form of argument. We will be ready to proceed, gentlemen.

Mr. Cook: I have tendered this additional instruction in view of the Court's ruling, where it feels a fraud instruction should be given, in the inception of a policy, and I have given counsel a copy. This sets out the statutory section and states that the defendant has the burden of proving these kind of elements.

The Court: It may be tendered and the record will show it has been refused. (A. 250-255; R. 855-865)].